THE PRINCIPAL PIE
Greedy Ratings Agencies Take it All

I've been reading a government report – a weighty tome published in April of 2011, and am impressed by how much they got right. It's called "WALL STREET AND THE FINANCIAL CRISIS: Anatomy of a Financial Collapse", and it's a page-turner. In the introduction, these Committee members state: "The investigation found that the crisis was not a natural disaster, but the result of high risk, complex financial products; undisclosed conflicts of interest; and the failure of regulators, the credit rating agencies, and the market itself to rein in the excesses of Wall Street." This 646 page congressional investigation concludes that mortgage based securities were overvalued by the very people entrusted to audit them and this conflict of interest was largely to blame for the global financial tsunami that started with a little subprime meltdown. The report goes on to say: "The Subcommittee's investigation uncovered a host of factors responsible for the inaccurate credit ratings issued by Moody's and S&P….[they] were paid by the Wall Street firms that sought their ratings and profited from the financial products being rated. … The result was a race to the bottom."

Not everybody agrees. One acquaintance said that some blame rests with greedy buyers who flipped houses, suburban dwellers who were living large, borrowers with monstrous appetites for material goods, a group one might call American Dream Chasers. Seems to be a very small group of people whose negligible influence in the corridors of power could not have brought entire continents to their economic knees. But how to prove that?

First task – historical perspective – what are they now, what were they at the height of the meltdown, and what were they before the meltdown? The Mortgage Banker's Association publishes quarterly statistics on Delinquencies and Foreclosures. Let's focus specifically on one-to-four residential properties.

2011 – Third Quarter Delinquency Rate : 7.99%

2011 – Third Quarter In-Foreclosure Rate : 4.43%

2009 – First Quarter Delinquency Rate : 8.22%
2009 – First Quarter In-Foreclosure Rate : 3.85%

2004– Second Quarter Delinquency Rate : 4.43%
2004– Second Quarter In-Foreclosure Rate : 1.16%

Second task - what is the dollar effect of these percentages? How big a piece of a banker's principal pie do they eat? The Federal Reserve releases a Statistical Supplement every quarter called "Mortgage Debt Outstanding", again focusing on just the one-to-four residential properties:
2011 – Third Quarter = $10.336 trillion dollars

2009 – First Quarter = $11.031 trillion dollars
2004 – Second Quarter = $7.571 trillion dollars
The portion of bad mortgages – the percentage of a ten trillion dollar pile of money that went into Foreclosure - rose from 1% to 4% over the last seven years. That's a record increase,

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but if we take 2011's third quarter for example, if every single foreclosure was completed, the potential loss might be $457 billion dollars. Typically, however, banks do realize an average of 50% of their principal owed, so it's more like $228 billion.

Commercial banks and savings institutions insured by the Federal Deposit Insurance Corporation (FDIC) reported an aggregate profit of $29 billion in the first quarter of 2011. One year's profits – one year – would suffice to reduce the principal on all homes currently being foreclosed upon by 25%. Imagine how much lower monthly payments could be then. If the banks had been truthful about the true worth of these assets, the concentric circles of misery generated by the dirty pebble thrown would never have spread beyond a few quarters of less than stellar banking profits.

Useful Inernet Links:

Permanent Subcommittee on Investigations: Anatomy of a Financial Collapse

https://www.fdic.gov/news/news/press/2011/pr11091.html

https://www.federalreserve.gov/econresdata/releases/mortoutstand/current.htm

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